

In order to compare the audience appeal of network programs with the substituted entertainment programs of affiliate preemptions, we examined the ratings of all one-time-only preemptions of CBS Television Network programming during the 1990/91 television season in 26 "metered" markets.^{47/} Although there is obviously no sure way to know how a network program would have performed on a particular station had it not been preempted, we chose to examine one-time-only preemptions because in each case there is a network program in the same time period, one week earlier and one week later, the ratings performance of which may be compared with the ratings performance of the affiliate's substituted program.

What we found is that for the average one-time-only preemption for entertainment programming, the network program in the same time slot one week earlier received a rating 24.1 percent higher; and that the network program in the same time slot one week later received a rating 27.8 percent higher.

47/ The "metered markets" are those geographic markets where the Nielsen Company measures ratings year-round by meters attached to television sets.

Thus, we estimate that on average a preempted network program would have drawn an audience approximately 25 percent greater than that received by the program substituted in its place. Only a severe marketplace distortion can explain why an affiliate would accept so significant a reduction in audience in order to run conventional entertainment fare.

C. The Incentive For Affiliates To Substitute Conventional Entertainment Programming For Network Programming Of Significantly Greater Audience Appeal Derives From An Artificial Flatness In Network Compensation Schedules Imposed by the Commission.

Because compensation within any given daypart is generally spread evenly over the programs in that daypart, regardless of their individual value to the affiliate, compensation lost in any given preemption is small compared to revenues a substitute program can generate for the station.

A flat network compensation schedule is diseconomic. It does not reflect true value of individual clearances. The most valuable program clearances to a network are the last ones -- the ones that the affiliate gives most reluctantly. The first clearances -- the programs that the

affiliate most wants to clear -- would, in a free market, be the clearances a network would pay the least for.

Thus, in a free market, one would expect the compensation schedule of an established network to be graduated, to a greater or lesser degree, so that each additional clearance (or batch of clearances) triggered a higher per program compensation payment than the clearances that went before it.

Thirty years ago, the Commission reviewed a compensation plan that had then been established by CBS. The plan called for network compensation payments equaling only ten percent of an affiliate's network rate up to a certain level of clearances, and then 60 percent of the station's network rate for all clearances above that level.^{48/}

The effect of the CBS plan was to pay for the last third or so of clearances at a rate slightly less than the rate syndicators were then paying for station time. (The syndication rate was then generally about 65 percent of a station's network rate.) CBS stated that its primary

48/ Columbia Broadcasting System, 22 R.R. 265 (1961).

purpose in adopting the plan was to compete against syndicators more effectively for clearances, but that it also wished to improve clearances as against the programs of other networks in one and two station markets.^{49/}

The Commission struck down the CBS plan, holding that it discouraged affiliates from clearing the programs of other networks and thus violated the rule against exclusive affiliation. The Commission observed that because the plan enabled CBS to pay high compensation rates at the upper level of hours taken, other networks would have difficulty competing for clearances on primary CBS affiliates.^{50/}

When CBS modified the plan to exclude preemptions for the programs of other networks, the Commission ruled that the plan, as revised, nonetheless discouraged preemptions for syndicated programs and thus violated the right-to-reject rule. Although the plan involved a compensation payment, at the upper end, that was comparable to the amount a syndicator would pay for the same clearance, the Commission objected to the fact that the

49/ Id.

50/ Application of Section 3.658(a) of the Commission's Rule, 23 R.R. 769 (1962).

plan "achieves [this] parity only by virtue of withholding a part of the normal compensation [at lower clearance levels]."51/

In rejecting the CBS compensation plan, the Commission stated that:

"any plan that provides for payment wherein the average hourly rate of compensation varies greatly or is heavily influenced by the number of hours taken has a coercive effect and tends toward full-line forcing."52/

The Commission cited with approval the statement by the Network Study Staff in its 1957 Network Study Report that "[i]n order to minimize the relationship between compensation and clearances, the most desirable compensation arrangement would be a flat percentage rate with no free hours."53/

The Commission's ruling in this case has had a lasting, dramatic impact on the structure of network compensation

51/ Application of Section 3.658(a) and (e) of the Commission's Rules, 24 R.R. 520a, 520f (1962).

52/ Application of Section 3.658(a) and (e) of the Commission's Rules, 24 R.R. 513, 515 (1962).

53/ Id. at 266, citing Network Study Report at 647.

plans. Because of this ruling, compensation plans have generally failed to reflect the economic realities of the network/affiliate distribution system. As a result, the efficiency of this distribution system on which free television depends has been measurably reduced, leaving broadcasting all the more vulnerable to competition from subscriber-supported systems.

However, the Commission's rationale for its CBS Compensation Plan ruling has no application to the modern video marketplace. It has been swept away by thirty years of dynamic growth. Today, the public interest is not advanced, but harmed, by the marketplace intervention accomplished by the Commission's three-decade-old decision against graduated compensation plans.

D. There Is No Longer Any Basis For Barring Networks From Negotiating Reasonable Financial Incentives For Affiliates' Clearances.

When the FCC ruled against CBS's "incentive compensation plan" three decades ago, it was quite possible to believe that any compensation plan that offered meaningful financial incentives for clearances was not in the public interest. As of 1960, there were only 514

commercial broadcast television stations in the United States,^{54/} many of them located in markets of only one or two commercial stations. As a result, in many markets the ABC Television Network in particular had to accept secondary affiliations from stations that were primarily affiliated with one of the two more established networks -- CBS and NBC.^{55/} For its clearances ABC depended to a significant degree on the non-clearance of CBS and NBC programs.

In this environment, there seemed much to gain in a marketplace intervention that promoted clearances of the programs of a struggling network, and little at stake in preventing the two solidly profitable networks from bargaining for the most efficient distribution of their programming.

A similar situation obtained with respect to syndicated programming. Given the paucity of stations at the time,

54/ Network Inquiry Special Staff, Final Report, Vol II, 1980 at 79.

55/ In 1960, the ABC Television Network had only 87 affiliates, compared with 214 for NBC and 195 for CBS. Network Inquiry Special Staff, Final Report, Vol. II, at 79, 83, 87.

there were few markets with independent stations.^{56/}
Non-clearance of network programming offered an important opportunity for presentation of non-network programs.

Thus, in striking down the CBS incentive compensation plan, the Commission emphasized the impact of a graduated compensation plan in markets where the three networks competed for airtime on only one or two commercial stations, and the importance of network preemptions by affiliates as a means by which syndicators obtained outlets for their programs.^{57/}

All this, of course, has changed dramatically. The number of commercial stations has doubled.^{58/} Dual affiliations are rare, and where they do occur the three original networks now face each other as true competitive

56/ As late as 1969 there were only 14 markets in the United States with at least one independent VHF station. (UHF stations suffered a severe competitive handicap in intermixed markets in the 1960's, before Congress required television sets sold in the United States to have UHF reception capacity.) See Competition and Responsibility in Network Television Broadcasting, 23 F.C.C.2d 382 (1970).

57/ Application of Section 3.658(a) and (e) of the Commission's Rules, 24 RR 513 (1962).

58/ As of 1990, there were a total of 1093 commercial television stations in the United States. OPP Working Paper at 15.

equals. The new Fox network has its own affiliates in markets covering 94 percent of the country,^{59/} and has looked to cable affiliations, rather than secondary affiliations with the affiliates of other networks, to cover the gap.

The growth in commercial television stations has also radically altered the syndication market. In the last decade alone the number of independent stations has tripled. As of 1990 there were 380 independent commercial stations in the United States, representing about 35 percent of all commercial television stations.^{60/} Thus, by 1990, 94 percent of television households were in markets with at least five television stations, typically including at least one independent station.^{61/}

Broadcast television has now become such a voracious consumer of programming that there is barely enough to go around. In this new environment, no network relies on preemptions by its rivals affiliates in order to survive.

59/ 1991 Nielsen Television Index.

60/ OPP Working Paper at 16.

61/ Id. at 17.

Now all are struggling and all rely on the same thing -- maximizing the clearances by their own affiliates.

And syndicators no longer depend on network preemptions to get their own programs on the air. The average affiliate has in the prime time "access" period alone approximately 26 hours each month of non-network time to fill. The other dayparts in an affiliate's schedule offer even more extensive opportunities for syndicators. And, of course, independent stations offer the most extensive opportunities of all.

Coincident with the growth in independent stations has been a sharp rise in the revenues from syndication, from roughly \$50 million dollars in 1980 to \$1.2 billion dollars in 1990.^{62/} Network preemptions -- which fluctuated during the decade but always within the same order of magnitude -- obviously had little if any bearing on this phenomenal growth.

Thus, the competitive concerns -- both inter-network and network-syndicator -- that underlie the CBS

62/ "Cosby Sidesteps Networks With His Biggest TV Deal," New York Times, October 28, 1991, at D8.

Compensation Plan decision are no longer valid. Today, an artificially flat compensation schedule serves only to undercut the viability of network broadcasting. Only a free market will allow broadcast distribution to achieve rational contours. Only a free market can provide broadcast television with the most efficient possible mix of network and syndicated programs -- the mix that will maximize the viability of networks, affiliated stations and independent stations.

As with cable networks, the clearance arrangements for broadcast television networks should be freely negotiated -- certainly as regards compensation payments.

III. THE PORTION OF THE PRIME TIME ACCESS RULE PROHIBITING AFFILIATES IN THE TOP-50 MARKETS FROM BROADCASTING OFF-NETWORK PROGRAMS DURING "ACCESS" PERIODS SHOULD BE REPEALED.

The prime time access rule provides that, with specified exceptions, television licensees in the top 50 markets may broadcast no more than three hours of network programming or off-network programs during the four evening hours that constitute prime time.^{63/}

CBS does not here challenge the rule limiting prime time network programming to three hours on top-50 market affiliates. We, do, however, challenge the rule's prohibition against the broadcast by top-50 market affiliates of off-network programs during the "access" period.

The off-network prohibition raises the costs of broadcast networking in two important ways: first, by artificially hobbling the ability of network affiliates to compete for viewers during "access" periods; and secondly, by artificially raising the cost to networks of the programming that they purchase. This harm to free television is not offset by any public benefit whatsoever.

63/ See 47 C.F.R. § 73.658(k).

Indeed, the PTAR restriction on off-network programming accomplishes nothing but to harm broadcast networks and their affiliates.

A. The PTAR Proscription On Off-Network Programming Pointlessly Reduces The Competitive Vitality Of Network Affiliates

By prohibiting top-50-market network affiliates from selecting off-network programs for their "access" schedules, the PTAR rule seriously diminishes the ability of these stations to compete effectively against both independent broadcast stations and non-broadcast alternatives such as cable.

Off-network programs generally are television's vintage best -- the expensively produced programs that, as first-run network series, were able to achieve a level of popularity sufficient to permit their survival for numerous seasons of network exhibition. By contrast, first-run syndicated programming is less expensively produced and is generally brought onto market without the benefit of an established public following. Therefore, it is not surprising that off-network programming newly introduced to syndication generally attracts far larger audiences than

first-run programming entering the syndication market for the first time.^{64/}

The inability to schedule off-network programs in the crucial "access" period hobbles the affected affiliates not only because those programs are often superior in their audience appeal, but also because these off-network programs are often the syndicated fare most compatible with the network programming schedule for the same evening. Scheduling programs of consistent demographic appeal can be crucial to building an evening's program-to-program audience flow. Therefore, the size of audiences for network programs can be directly affected by the character of affiliates' "access" programming. A rule that has the effect of restricting top 50 market affiliates to a menu of inexpensive game shows and "reality" magazines reduces the competitive vitality of both broadcast networks and their affiliates.

B. The Natural Effect Of The Rule's Off-Network

^{64/} See, e.g., "Off-netters Top Syndie Ranks," Variety, October 28, 1991, at 23.

Proscription Is To Raise The Price To Networks Of The
Programming That They Purchase.

In adopting the prime time access rule, the Commission noted that "[i]n many cases packagers do not recover the costs from the network run of a program series, but must look to profits from domestic syndication, foreign sales and other subsidiary uses of the series to recover their costs and make a profit..."^{65/} The deficit financing of prime time network series by their producers is commonplace today as well.

To attain maximum value as a syndication prospect, a network series must have remained in production long enough to yield a "strippable" number of episodes -- the minimum of 65 or so programs necessary to fill a five-nights-a-week schedule. The relatively few episodes that are produced during a limited network run of a series will, in all likelihood, not be enough for significant aftermarket use.

But if a network series survives -- if it remains on the network schedule long enough -- the producer has the

^{65/} Competition and Responsibility in Network Television Broadcasting, 23 F.C.C. 2d 382, 389 (1970).

opportunity to receive an excellent return on the capital he has risked.^{66/} Obviously, the amount of deficit financing that a producer is willing to gamble is a function of the likelihood of the program's succeeding and the size of the return he can expect if the program does succeed. Anything that reduces that potential return raises the price a network must be willing to pay to get the program produced.

By removing off-network programming from the access schedules of top 50 market affiliates, the PTAR rule significantly reduces a producer's potential return on that programming. This is because of all dayparts, the number of homes using television ("HUTs") is highest during prime time. Of the various time periods when network affiliated stations typically schedule non-network programming, there is none with a greater audience potential than the "access" period. Thus, in May 1991 the HUT level in the top 50 markets was approximately 50 percent higher in the "access" period (generally 7-8 PM ET) than in the "early fringe" period (generally 4-5 PM ET) -- the time before local news

^{66/} See, e.g., "Cosby Sidesteps Networks With His Biggest TV Deal," New York Times, October 28, 1991, p. D1.

programs when stations generally broadcast syndicated programs.^{67/}

There are also many off-network series which, by their nature, appeal to an audience that is most likely to watch television during prime time. This is particularly true of programs with a strong appeal to adults. For example, in those markets where the results are unaffected by the PTAR rule (i.e., those markets other than the top 50), the three top rated syndicated off-network series in May 1991 -- MASH, GOLDEN GIRLS, and WHO'S THE BOSS -- each averaged a rating of 10.0 or above when scheduled in prime access, but ratings of only 3.6, 6.8 and 5.5, respectively, when scheduled in the early fringe period.^{68/} Thus, the potential advertising revenues that a station can expect to generate by broadcasting each of these three programs (and most other off-network programs) turns largely on when during the day the program is scheduled.

By barring off-network programs from "access" periods, the PTAR inevitably reduces the amount that a top 50 market

67/ Source: A.C. Nielsen. See Exhibit I annexed.

68/ For a comparison of the ratings performance of eleven syndicated off-network series in the "access" and "early fringe" dayparts, see Exhibit II, annexed.

affiliate can bid for an off-network program. Three potential high-bidders are effectively removed from the auction for the best off-network series, thus inevitably depressing the after-market revenues that these series can generate.

The off-network restriction also reduces the opportunity to exploit the value of a moderately successful network series and thereby raises the producer's risk and the network's costs. If a series has had a significant network run, but not one sufficient to produce the minimum of 65 or so programs necessary to fill a five-nights-a-week schedule in syndication, the producer may attempt nonetheless to fill out the minimum complement of programs that will permit the series eventually to enter the lucrative "strip" syndication market. He may do this by keeping the series in production for first-run syndication or cable until he has generated a "strippable" number of programs. In the recent past, this has been done with a number of former network series such as BAYWATCH, FAME and THE DAYS AND NIGHTS OF MOLLY DODD.

The Commission, however, has made clear that those episodes in a series that once ran on a network are covered by PTAR's off-network proscription, no matter how many

other episodes in the same series never had a network broadcast.^{69/} The Commission has also held that the off-network restriction applies to program elements from a network series even when incorporated into new programs.^{70/} This has substantially diminished the potential value of network variety programs. Top 50 market affiliates are barred from broadcasting during their "access" periods new variety anthology programming that incorporates the brilliant comedy sketches of YOUR SHOW OF SHOWS, the virtuoso performances of THE ED SULLIVAN SHOW, or any other vintage variety material. This fact certainly has not enhanced the willingness of producers to invest in quality variety programming, and that particular form has largely migrated to cable.^{71/}

69/ See, e.g., Rhodes Productions, Inc., 58 RR 2d 126 (1985).

70/ Id.

71/ Until 1975, the Commission did occasionally grant "off-network" waivers for the network episodes of some, but only some, series. Thus, the Commission permitted access syndication of all episodes (including off-network episodes) in the WILD KINGDOM, NATIONAL GEOGRAPHIC, ANIMAL WORLD and SIX WIVES OF HENRY VIII series, but not the LASSIE, HOGAN'S HEROES or MR. MAGOO series. See 33 FCC 2d 583, 35 FCC 2d 758, 29 RR 2d 754, 25 RR 2d 793, 37 FCC 2d 933, 29 RR 2d 754 and 31 RR 2d 409. The Commission's strained explanations for why some programs and not others were receiving favorable treatment did little to allay the suspicion that the difference derived entirely from

(Continued on Page 64)

Quality television that is free to the consumer cannot survive unless producers of quality programs are willing to sell broadcast rights at prices that networks can afford -- prices that can be offset by advertising revenues. By artificially depressing the potential rewards of off-network syndication, the rule poses a serious, and utterly pointless, impediment to the survival of free first-quality television.

C. The PTAR Rule's Off-Network Proscription Artificially Biases The Television Programming Market Against Established Networks And In Favor Of Cable Networks And New Broadcast Networks.

At a time when the future of the three established broadcast networks as distributors of first-quality programming is in serious doubt, there is no justification for regulatory intervention with no significant effect except to prejudice the ability of these networks to

71/(Continued from Page 63)

the Commission's evaluation of the content worthiness of each program. Indeed, this series of decisions is a striking illustration of how easily the hyperregulation of broadcasting lapses into content control. When the Court of Appeals criticized this pattern of waivers "issued on and ad hoc basis, without any formulated regulations such as would be required in good administrative practice," the Commission stopped issuing them entirely. National Ass'n of Independent Television Producers and Distributors v. FCC, 516 F.2d 526, 537 (2d Cir. 1975).

compete effectively against their main challengers -- cable networks and new broadcast networks. The PTAR rule's off-network restriction amounts to just such an intervention.

When producers sell exhibition rights to a cable network they know that the program they are producing has the possibility of enjoying a lucrative afterlife as a strip-syndication access series. The same is true of a sale to the Fox network or any other new broadcast network that is protected from application of PTAR by the "15 hour" definition of a network that the Commission adopted for the rule.^{72/}

72/ As originally enacted, the rule applied to all broadcast networks. Competition and Responsibility in Network Television Broadcasting, 23 F.C.C. 2d 382 (1970). The Commission subsequently amended the rule to apply to only "major national television networks" in order to allow affiliates to fill the access period with programming from networks other than ABC, CBS and NBC. Competition and Responsibility in Network Television Broadcasting, 25 F.C.C.2d 318 (1970). The rule currently applies only to those networks "providing on a regular basis more than fifteen (15) hours of prime time programming per week (exclusive of live coverage of bona fide news events of national importance) to interconnected affiliates that reach, in aggregate, at least seventy-five (75) percent of television households nationwide..." 47 C.F.R. Section 73.662(i).

Thus, for example, the producer of the Fox comedy series MARRIED WITH CHILDREN has been able to syndicate that program to any station in any market for broadcast in any time period, including the access period. This is an enormous advantage to a producer, and one which undoubtedly affects the price at which programs are offered to Fox as compared to the price that ABC, CBS or NBC must pay. Yet there is no logical basis for distinguishing MARRIED WITH CHILDREN from any other network situation comedy -- certainly no difference calling for preferential governmental treatment.

Just last year Fox itself highlighted the importance of the off-network proscription when it sought a limited waiver of the "15 hour" rule defining those "networks" to which PTAR and the financial interest and syndication rules apply.^{73/} The waiver Fox sought went only to the off-network aspect of PTAR, Fox and its affiliates having agreed to comply with the rule's limitations on prime time

73/ Fox Broadcasting Co., Request for Temporary Waiver of Certain Provisions of 47 CFR Section 73.658, 67 R.R. 2d 1086 (1990). At the time Fox sought this waiver, the rule defined a "network" in terms of its transmission of 15 hours of programming weekly in all dayparts to 25 or more affiliates in 10 or more states, an hourly program total which Fox then anticipated exceeding.

network programming even if the waiver were granted.^{74/}
There is no doubt that Fox and its affiliates perceived relief from the off-network proscription as vital to their operations.^{75/}

The Commission did grant the waiver Fox sought, thus permitting the Fox network for one year to transmit up to a total of 18 1/2 hours per week of network programming without that programming incurring the liability of the "off-network" classification. The Commission identified as one of its primary considerations in granting this relief its desire to "promote new networks."^{76/}

We are not opposed to the Commission's goal of promoting new networks. However, we believe the time has come for the Commission to promote old networks as well. At the very least, if the PTAR off-network proscription is retained, it should be applied on an equal basis to the

74/ Id. at 1087.

75/ The Fox affiliates argued that they had expensive inventories of off-network programming "which had been purchased because of the uncertain outcome of this waiver request and the related rulemaking proceeding, the cost of which programming "could not [be] recover[ed] during any other part of the day [but the access period]." Id. at 1090.

76/ Id. at 1087.

programming of all networks -- broadcast (old), broadcast (new) and cable.^{77/}

D. The PTAR Bar On Off-Network Programming Does Not Serve The Purpose For Which It Was Enacted.

The prime time access rule, originally proposed by the Westinghouse Broadcasting Company, was initially rejected by the Commission in 1963 on grounds that it entailed too great a "restraint on the licensee's freedom of choice with respect to programming his station."^{78/} By 1970, however,

^{77/} Last May, the Commission decided to permit networks to syndicate programming produced "in-house" or under certain co-production arrangements. Financial Interest and Syndication Rules, 6 FCC Rcd at 3118-20. The Commission did so in the interest "of giving the networks a greater opportunity to control their production costs and reap the rewards from substantial investments in programming." Id. at 3116. This goal, of course, would be substantially undermined by the continued existence of the PTAR ban on off-network programming, which significantly depresses the potential off-network syndication revenues for network-produced programs.

^{78/} Option Time and the Station's Right to Reject Network Programs, 34 F.C.C. 1103, 1131 (1963).

the Commission decided that the benefits of the proposal outweighed this detriment and enacted the rule.^{79/}

Specifically, by adopting the rule the Commission hoped "to multiply competitive sources of television programming"^{80/} and "to open access to the valuable nighttime hours to independent producers."^{81/} The Commission stressed that its intervention in the program schedules of network affiliates was required if first-run syndicated programming was to have an opportunity for prime time exposure given the paucity of alternative outlets. Thus the Commission stated that:

"[t]he facts which propel us to action are relatively simple and, we believe, quite compelling. ... [A]s of December 31, 1969...the United States as a whole had 621 stations, of which 499 were network affiliates. Of the top 50 markets only 14 had at least one independent VHF television station. In the prime evening hours, control over programming and over access to the licensed television stations is heavily concentrated in only three hands."^{82/}

The Commission also cited "the virtual disappearance of

79/ Prime Time Access Rule, 23 F.C.C.2d 382 (1970).

80/ Id. at 382.

81/ Id. at 384.

82/ Id. at 385.